

The background of the entire page is a close-up, slightly blurred image of the American flag, showing the stars and stripes in a diagonal orientation.

Federal Communications Commission

OFFICE OF THE INSPECTOR GENERAL

Semiannual Report to Congress

April 1, 2006 – September 30, 2006

Kent R. Nilsson
Inspector General

MEMORANDUM

OFFICE OF INSPECTOR GENERAL

MEMORANDUM

DATE: October 31, 2006

**REPLY TO
ATTN OF:** Inspector General

SUBJECT: Semiannual Report

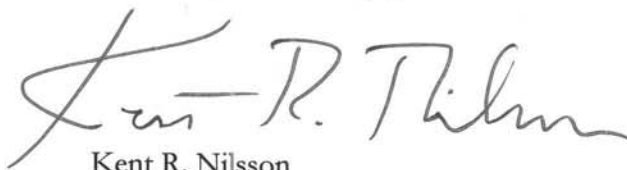
TO: Chairman, Federal Communications Commission

In compliance with Section 5 of the Inspector General Act, as amended, 5 U.S.C. App. 3, § 5, I respectfully submit the Office of Inspector General (OIG) Semiannual Report summarizing the activities and accomplishments of the OIG during the six-month period ending September 30, 2006. In accordance with Section 5(b) of the Act, it would be appreciated if this Semiannual Report, along with the report that you prepare as Chairman of the Federal Communications Commission (FCC), were forwarded to the appropriate Congressional oversight committees within thirty days of your receipt of this report.

During this reporting period, as in the previous one, OIG activity continued to focus on Universal Service Fund activities. Our efforts in this area have been summarized in a special section of this report entitled "Oversight of the Universal Service Fund."

This report describes audits that are in process, as well as those that have been completed during the preceding six months. OIG investigative personnel continued to address issues referred to, or initiated by, this office. Where appropriate, investigative reports have been forwarded to the FCC's management for action.

This office is committed to maintaining the highest possible standard of professionalism and quality in its audits, investigations, inspections and consultations and we welcome any comments or suggestions that you might have. Please let me know if you have any questions or comments.



Kent R. Nilsson
Inspector General

Enclosure
cc: Chief of Staff
Managing Director



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INTRODUCTION

The Federal Communications Commission (FCC) is an independent regulatory agency, which was delegated authority by Congress to regulate interstate and foreign communications by radio, television, wire, satellite and cable. The FCC's jurisdiction covers the fifty States, the District of Columbia and all U.S. territories.

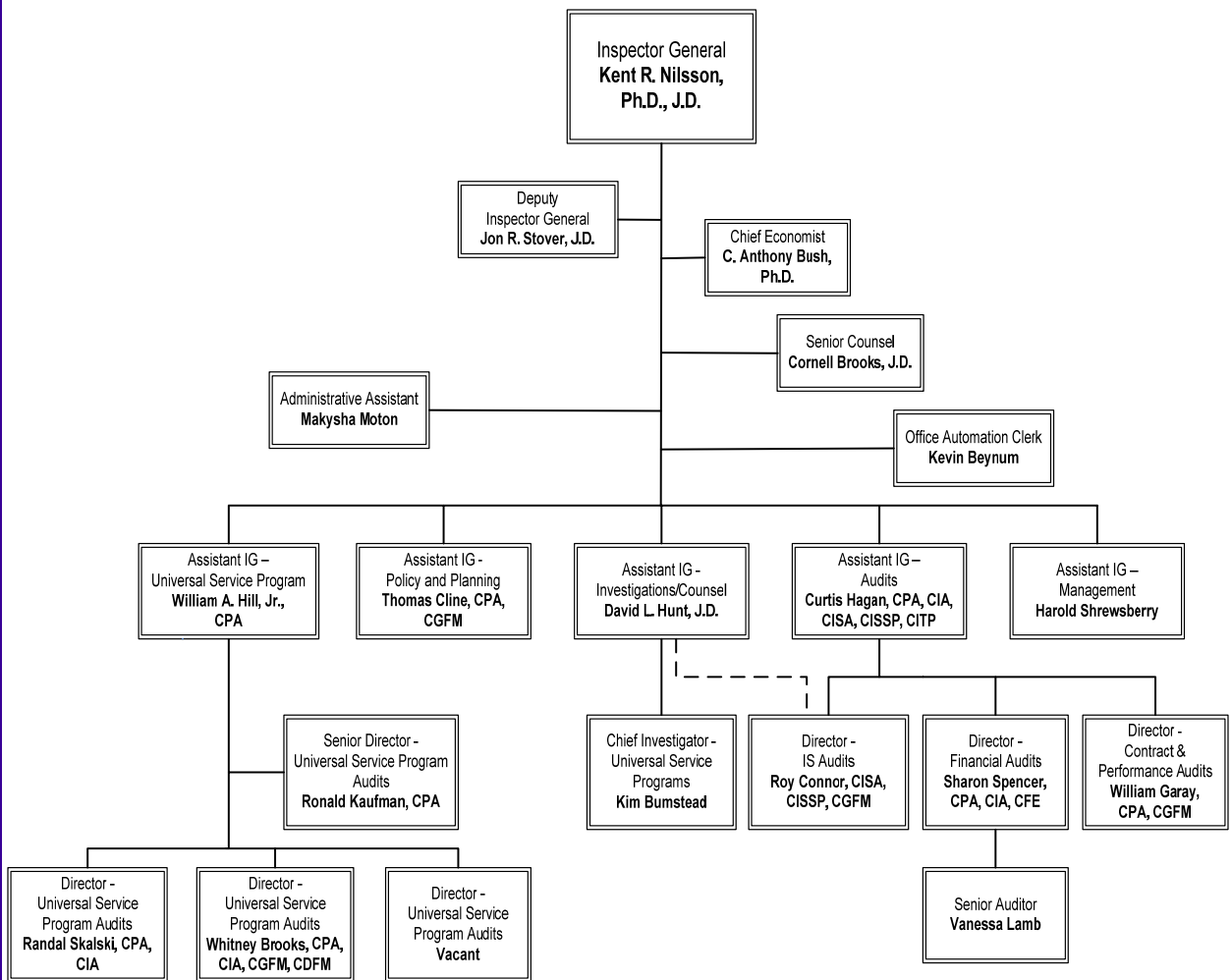
The FCC consists of a Chairman and four Commissioners, who are appointed by the President and confirmed by the United States Senate. Kevin J. Martin serves as Chairman. Michael J. Copps, Jonathan S. Adelstein, Deborah Taylor Tate and Robert M. McDowell serve as Commissioners. Most of the FCC's employees are located in Washington, D.C. at the Portals II building, which is located at 445 12th St., S.W., Washington, D.C. 20554. FCC field offices and resident agents are located throughout the United States.

The Office of Inspector General (OIG) is dedicated to assisting the Chairman in his continuing efforts to improve its effectiveness and efficiency. The Inspector General (IG), Kent R. Nilsson, reports directly to the Chairman. The OIG staff consists of 19 professionals. Principal assistants to the IG are: Jon R. Stover, Deputy Inspector General; David L. Hunt, Assistant Inspector General (AIG) for Investigations/General Counsel; Curtis Hagan, AIG for Audits; William A. Hill, Jr., AIG for Universal Service Fund Oversight; Thomas Cline, AIG for Policy and Planning; and Harold Shrewsbury, AIG for Management.

This semiannual report includes the major accomplishments and activities of the OIG during the period from April 1, 2006 through September 30, 2006, as well as relevant information on the OIG's goals and future plans.

OIG MANAGEMENT ACTIVITIES

As noted above, this office currently has a **OFFICE STAFFING** staff of 17 permanent employees and a full complement of Assistant Inspectors General (“AIGs”). We did not, however, begin the reporting period in this position. At times during the last six months, many AIG and staff auditor positions were vacant. With the support of the FCC’s Chairman and his staff, I was able to hire a number of employees that is unprecedented in the history of this office, including additional staffing allocations for the USF team. The addition of a Chief Economist and a Senior Counsel provides this office with statistical and legal capacity that will be highly valuable in both audits and investigations in the coming months. Following is the organization chart for the office:



OIG MANAGEMENT ACTIVITIES

In the OIG's fiscal year 2007 budget request, the IG requested 16 additional staff positions to support and perform quality assurance for audits in the Universal Service Fund (USF) area. These resources, however, have not been provided through the legislative process although they were recommended by the Chairman and included in the President's budget. For FY2008, we have requested additional staff positions and other resources. The Chairman has also supported this request and the Office of Management and Budget included a request for \$20.4 million and 12 FTE staff positions in the President's 2007 budget request. We have also requested additional information technology specialists, investigators, and attorneys due to a dramatic growth in investigative activities. Chairman Martin has also supported this request.

Our staff is made up of seasoned professionals, most of whom have one or more professional certifications. We support the efforts of our staff to expand their bodies of knowledge and professional recognition, and the Chairman has funded examination preparation for the Certified Public Accountant and Certified Information System Security Professional designations. In our continuing effort to increase the expertise of our audits and investigative staff, members of this office have also attended training at the Inspector General Criminal Investigative Academy, other Federal Inspector General training events, master's level classes at colleges and universities, other technical seminars, and the Inspector General completed additional executive training at the Federal Executive Institute.

OFFICE MODERNIZATION

An analysis of existing information technology systems was performed to identify new equipment requirements for the additional staff. This analysis concluded that the OIG lagged behind the rest of the Federal government with its then current information

processing technology. The IG made a decision to modernize the OIG to insure that the OIG has the technological capability to process and manage the volume of audits and investigations planned for the Universal Service Fund, other OIG audit areas, and

OIG MANAGEMENT ACTIVITIES

an increasing number of investigations in other areas.

This modernization project started with the acquisition of Blackberries and cell phones for all professional staff and continued with new notebook and personal computers that contain the latest versions of applications that enhance productivity and performance. Tablet computers are being acquired for personnel who are frequently on travel. The procurement of a new color printer, digital scanner and portable printers further improves the OIG information processing capabilities. This stage of the modernization project brings the OIG closer to the quality of information technology systems that is necessary for the Office to perform its statutory responsibilities.

The second phase of the modernization project will include the purchase of an advanced management software system that will permit audit tracking, audit resolution, investigation case management, integrated workflow management, employee time tracking, contract management support, and office management support operating in a secure environment. The system will be specifically designed to manage audits, investigations, inspections, surveys, and special studies. An additional aspect of this project will include an expansion of our investigative capabilities with the purchase of computer forensic hardware and software, along with technical training in the use and management of these tools.

The OIG welcomes college interns during the fall, spring and summer semesters. Most of these students take their internships for credit. Recent interns have come from schools across the country including American University, Arizona State University, DePauw University, Georgetown University, Hamilton College, James Madison University, Long Island University, North Carolina State University, Purdue University, the University of California at Berkeley, the University of California at Davis, the University of Maryland Law School, the University of North Carolina, and Xavier University.

INTERNSHIP PROGRAM

OIG MANAGEMENT ACTIVITIES

These internships have proven to be rewarding experiences for all participants. Students leave with a good understanding of how a government agency operates, and they have the opportunity to encounter challenges while enjoying the rewards that can come from public service. In turn, the Office has benefited from the students' excellent work performance that, in part, has reflected their youth, exuberance, and special skills.

LEGISLATIVE & POLICY MATTERS

Pursuant to section 4(a)(2) of the Inspector General Act of 1978 (IG Act), 5 U.S.C.A. App. 3 as amended, our office monitors and reviews existing and proposed legislative and regulatory items for their impact on the

OIG and the FCC's programs and operations. Specifically, we perform this activity to evaluate their potential for encouraging economy and efficiency while helping to reduce fraud, waste, abuse, and mismanagement.

The office continued to monitor legislative activities affecting the activities of the OIG and the FCC during this period. This office specifically monitored legislation and legislatively related proposals that, directly or indirectly, affect the ability of Designated Federal Entity IGs to function independently and objectively.

Additionally, the OIG continuously monitors FCC policy development and provides input as appropriate. In particular, OIG input into policy and procedures on matters that directly relate to audit and oversight of agency functions and programs has been sought and considered by the FCC's management. During the reporting period, we provided input into draft directives for audit follow-up (a revision to existing procedure), anti-fraud measures (a new procedure), and guidance to the Universal Service Administrative Company (USAC).

AUDIT AREAS

Beginning with the Inspector General's semiannual report for the period ending March 31, 2002, the IG has included a section that

covers the office's efforts to oversee the Universal Service Fund (USF). Due to its materiality and an initial assessment of its potential for waste, fraud and abuse, this office had previously focused much of its effort on the USF mechanism for funding telecommunications and information services for schools and libraries, also known as the "Schools and Libraries Program" or the "E-rate" program.

In this report, we provide an update on our oversight activity during the most recent six month reporting period, and also provide information concerning a much greater effort that has been initiated by the Inspector General that involves all USF programs. In addition to the schools and libraries program, the IG has now expanded our audit efforts into the high cost, rural health care and low-income programs as well as audits of contributors to the program. In this section, we provide an update on our oversight activities; provide an update on audits being conducted by other Federal Offices of Inspector General on our behalf; and summarize other significant investigative activity.

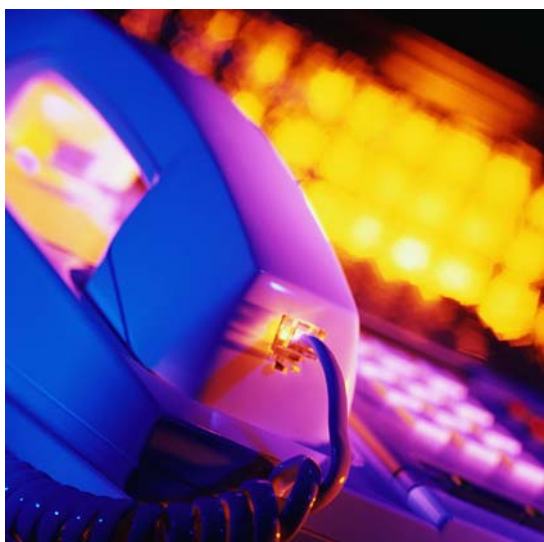
As discussed in previous reports, the primary obstacle to an effective, independent oversight program has been, and continues to be, inadequate audit and investigative resources so that OIG can conduct its own audits and provide adequate audit support to investigations. This continues to be true. The IG, however, has been able to hire two additional employees to oversee the new audit initiative currently underway and Chairman Martin and his staff have been instrumental in working with the IG to provide additional resources. Chairman Martin continues to support our effort to acquire additional funding and

UNIVERSAL SERVICE FUND (USF) OVERSIGHT

UPDATE ON OIG OVERSIGHT ACTIVITIES

AUDIT AREAS

resources and has requested funds to provide our office with the necessary funding to support the work of this office. Inadequate investigative and internal audit resources have prevented the OIG from fully completing the body of work it believes is essential to assessing fraud, waste, and abuse, which will continue to be the case until all the necessary resources are in place. In addition, inadequate resources have made it difficult for the OIG to provide requested support to Federal law enforcement in investigations of fraudulent activity in the E-rate program. This will become more pressing as the new audit initiative takes place and new referrals are added.



In the last semiannual report, the IG was able to state that progress had been made with the addition of two audit staff to the USF audit and investigations team. Since the President designated Kevin J. Martin as the new Chairman of the Commission, this office has been making steady progress in adding the necessary resources and will continue with this effort until we are adequately staffed to fulfill our responsibilities. Beginning with the Commission's FY

2007 budget submission, Chairman Martin requested, and the President included, an additional \$20,480,000 funded through USF program receipts. That request is still pending before Congress. With our budget request for FY 2008, we have asked for an additional funding from USF receipts.

In our last semiannual report to the Congress, we reported that we had been working with USAC to increase the number, and the quality, of USF audits to fulfill the statutory requirements required of the Commission as mandated by the Improper Payments Improvement Act of 2002 (IPIA). The OIG, with the help of the Commission's Office of Managing Director, decided to renew an option with KPMG, LLP to continue its work in the schools and libraries program. With the release of multiple Requests for Proposals (RFPs) in mid-June 2006, the OIG is overseeing an unprecedented num-

AUDIT AREAS

ber of audits of every component of the universal service program. Contributors and beneficiaries of the program including High Cost companies, Rural Health Care providers, Low Income recipients as well as Schools and Libraries will be subjected to the highest level of audit scrutiny and attestation opinion audits. After vigorous competitive bidding, independent public accounting firms submitted bids and nine were selected. Draft reports are scheduled to be completed by May 31, 2007, and final reports by July 31, 2007.

USAC continues to work with its contracted statistician from George Mason University and the statistician continues to work with the various accounting firms, USAC, and the OIG to develop an optimal statistical design to evaluate an error rate for erroneous payments in the various USF programs and contributions. The sampling design has been completed



for each of the four universal service programs as well as a sampling design to determine whether contributors are being properly charged. The work of USAC's statistician has been reviewed by FCC statisticians who, in addition, designed the sampling methodology and drew the audit samples for the rural health care and contribution audits.

As this new initiative takes place, the OIG and USAC continue to work through reviewing KPMG's previous 100 audits of the Schools and Libraries program. This body of work will be completed in the near future. To date, KPMG has issued 96 reports in draft and approximately 70 of these drafts have undergone USAC Internal Audit department or OIG's quality assurance review and have been presented to the appropriate parties for responses. We reviewed and released 53 audit reports in this reporting period that identified \$11,502,220 of potential improper payments that were made in

AUDIT AREAS

the Schools and Libraries program. The process to recover these funds is underway.

These audits identified several areas in which beneficiaries of USF funds have not complied with the Commission's rules. These audits also enable us to recommend changes to the FCC's management that will ensure the implementation of necessary controls to promote efficiency and to prevent fraud, waste, and abuse. A summary of the types of findings most frequently encountered in these audits are described in the following table:

Summary of E-rate Audit Findings	
<i>Program Area</i>	<i>Related Finding</i>
Technology Budget	The beneficiary did not have proper approval for its budget or an adequate amount budgeted for its share of the non-discounted costs.
Equipment	Equipment missing, not installed, no asset listing maintained, etc.
Discount Calculation	Beneficiary incorrectly calculated its discount percentage, could not support the discount, or could not provide documentation to verify information on the FCC Form 471.
FCC Form 472/474 Items	Errors in amounts for reimbursement, inadequate support, etc.
Children's Internet Protection Act	Beneficiary did not comply with the Children's Internet Protection Act.
Service Provider Billing	Bills not properly prepared or inaccurate.
Document retention	Beneficiary did not maintain the required documentation or documentation was non-existent.
Technology Plans	Beneficiary did not have an approved technology plan, technology plan was outdated, etc.
Ineligible Items	Beneficiary was reimbursed for ineligible products or services.
FCC Form 500	Beneficiary did not submit a Form 500 to USAC when the commitment was not fully utilized.

AUDIT AREAS

Following is a listing of the 53 audit reports, issued as of September 30, 2006.

Beneficiary	Location	Potential Improper Payment
Long Branch School District	Long Branch, NJ	\$0
Providence Public Schools	Providence, RI	\$0
Denver Public Schools	Denver, CO	\$0
Harlandale Independent School District	San Antonio, TX	\$13,700
Dallas Independent School District	Dallas, TX	\$0
Sunnyside Unified School District 12	Tucson, AZ	\$205,654
Clark County School District	Las Vegas, NV	\$0
Cincinnati City School District	Cincinnati, OH	\$988
Long Beach Unified School District	Long Beach, CA	\$0
Rhode Island Department of Elementary and Secondary Education	Providence, RI	\$47,865
Buchanan County School District	Grundy, VA	\$13,752
Fairfax County Public Schools	Fairfax, VA	\$0
Iowa Department of Education	Des Moines, IA	\$0
North East Independent School District	San Antonio, TX	\$2,122
Weslaco Independent School District	Weslaco, TX	\$215,995
Gallup-McKinley County School District	Gallup, NM	\$44,646
Dorchester County School District #4	Saint George, SC	\$36,053
El Monte City Elementary School District	El Monte, CA	\$15,941
San Bernardino City Unified School District	San Bernardino, CA	\$0
San Felipe – Del Rio City ISD	Del Rio, TX	\$22,677
Texas Youth Commission	Austin, TX	\$231,864
San Diego County Office of Education	San Diego, CA	\$12,273
Eastern Nebraska Distance Learning Consortium	Fremont, NE	\$26,273
Richland County School District	Columbia, SC	\$31,094
Aldine Independent School District	Houston, TX	\$50,708
American Samoa SEA	Pago Pago, AS	\$2,355,844
Bassett Unified School District	La Puente, CA	\$0
Stockton City Unified School District	Stockton, CA	\$21,558

AUDIT AREAS

Beneficiary	Location	Potential Improper Payment
Houston Independent School District	Houston, TX	\$72,962
Berkeley County School District	Moncks Corner, SC	\$0
School City of East Chicago	East Chicago, IN	\$27,907
Baltimore City Public School District	Baltimore, MD	\$2,533,007
LaJoya Independent School District	LaJoya, TX	\$551,581
Wilson School District 7	Phoenix, AZ	\$0
Dougherty County School District	Albany, GA	\$1,586
Leake & Watts Services, Inc.	Yonkers, NY	\$0
Desert Sands Unified School District	La Quinta, CA	\$106,994
Pomona Unified School District	Pomona, CA	\$0
Guam Department of Education	Hagatna, GU	\$82,390
Navajo Nation Library Consortium	Window Rock, AZ	\$28,722
Newark School District	Newark, NJ	\$503,508
Edinburg Independent School District	Edinburg, TX	\$17,446
Delano Joint Union High School District	Delano, CA	\$3,501,993
Charleston County School District	Charleston, SC	\$61,382
Garden Grove Unified School District	Garden Grove, CA	\$26,389
CENIC - Corporation For Network Education Initiative In California	Los Almitos, CA	\$425,402
Pasadena Independent School District	Pasadena, TX	\$0
Gadsden I.S.D.	Anthony, NM	\$59,373
Birmingham City School District	Birmingham, AL	\$0
Department of Information Systems State of Arkansas	Little Rock, AR	\$17,780
Norwalk La Mirada	Norwalk, CA	\$0
Columbus Public Schools	Columbus, OH	\$4,858
Palm Beach County School District	West Palm Beach, FL	\$129,933
Total Improper payments		\$11,502,220

AUDIT AREAS

In addition to all of the USF work efforts underway, the Commission has made changes in the roles and responsibilities of Bureaus and Offices, including the OIG. Several functions have been reorganized to meet the Commission's on-going goals of making the administration of the USF more efficient and effective. These changes have had a significant impact on the roles and responsibilities of the OIG regarding USF oversight. The new IG has made several key appointments including a new Assistant IG for Investigations and a new Assistant IG for USF Oversight. Chairman Martin has also provided communications equipment as well as computer hardware and software to support the field work of the OIG's auditors, investigators, and attorneys and has increased the training budget and travel funding of the OIG.

On January 29, 2003, the IG executed a Memorandum of Understanding (MOU) with the Department of the Interior (DOI) IG. This MOU

AUDITS CONDUCTED BY OTHER FEDERAL OIGS

was a three-way agreement among the Commission, DOI IG, and USAC for audits of schools and libraries funded by the Bureau of Indian Affairs and other universal service support beneficiaries under the audit cognizance of DOI OIG. Under the agreement, auditors from DOI OIG perform audits for USAC and the FCC OIG. In addition to audits of schools and libraries, the agreement authorizes the DOI OIG to consider requests for investigative support on a case-by-case basis. DOI OIG has recently submitted two audits to the OIG. One was an audit of the Bureau of Indian Affairs and the other was an audit of the Virgin Islands Department of Education. These audits have been completed and provided to the OIG staff. The OIG has completed its quality assurance review of these audits and has transmitted the reports to the responsible officials at USAC for comment.

We have also established a working relationship with the Office of Inspector General at the Education Department (Education OIG). In January 2004, the Education OIG

AUDIT AREAS

presented a plan for an audit of telecommunication services at the New York City Department of Education (NYCDOE). Because of the significant amount of E-rate funding for telecommunication services at NYCDOE, Education OIG has proposed that they be reimbursed for this audit under a three-way MOU similar to the existing MOU with DOI OIG. In April 2004, the Universal Service Board of Directors approved the MOU. In June 2004, the MOU was signed and the audit was initiated. The Education OIG held an exit conference with the NYCDOE on September 29, 2005 and forwarded its audit findings to the OIG during February, 2006. We anticipate transmitting this the draft report to USAC for its comments and issuing it in final during early FY 2007.



SUPPORT TO INVESTIGATIONS

In addition to the audit component of our oversight program, we have provided, and continue to provide, audit and investigative support to Federal investigations of E-rate

recipients and service providers. To implement the investigative component of our plan, we developed a working relationship with the Antitrust Division of the Department of Justice (DOJ). The Antitrust Division, in turn, has established a task force to conduct USF investigations that is comprised of attorneys in each of the Antitrust Division's seven field offices and the National Criminal Office. As of the end of this reporting period, we are directly supporting 26 investigations and monitoring an additional 11 investigations.

Significant accomplishments in investigative support include indictments, convictions, fines and negotiated settlements. Following are major accomplishments during the reporting period for which the OIG provided support.

- In April 2006, a Federal Grand Jury in the U.S. District Court for the District of

AUDIT AREAS

South Carolina indicted Cynthia K. Ayer on 12 counts of mail and wire fraud in an alleged scheme to defraud the E-Rate program. Ayer is the former director of technology for the Bamberg County School District One in Bamberg, SC. According to the indictment, Ayer used her position, between 1999 and 2003, to submit fraudulent applications for the E-Rate program and award technology contracts to her own company, "Go Between Communications."

- In April 2006, NextiraOne, LLC, a subsidiary of Platinum Equity, LLC, was sentenced to pay \$4.6 million in fines and restitution for defrauding the E-Rate program and the Oglala Nation Educational Coalition member schools on the Pine Ridge Reservation in South Dakota. According to the single-count wire fraud indictment filed in U.S. District Court in South Dakota, the illegal practices included inflating equipment prices, submitting false and fraudulent invoices for payment, and failing to install and deliver certain equipment and services originally billed to the E-Rate program. Nextira will pay a \$1.9 million criminal fine and a civil settlement requires the company to forfeit more than \$2.6 million in reimbursement for uncompensated work previously performed at other school districts.
- In May 2006, a Federal grand jury in the U.S. District Court for the Eastern District of Michigan indicted Douglas A. Benit and his wife, Mary Ann Elam Benit, for their role in an allegedly fraudulent scheme to obtain almost \$7.3 million from the Ecorse (MI) Public Schools and the E-Rate program. The nine-count indictment charges that Benit, a former Assistant Superintendent at Ecorse Public Schools' and his wife, used Benit's official position to steer contracts at the school district to Coral Technology Inc., an Ohio corporation under Benit's control. Charges against the Benits, Coral Technology, and another company under their control, School Management Services, Inc., a Michigan corporation, include conspiracy to commit Federal program fraud, mail fraud and aiding and abetting, wire fraud and aiding and



AUDIT AREAS

abetting, bank fraud and aiding and abetting, and conspiracy to commit money laundering.

- In June 2006, the state of Indiana and the Intelnet Commission, a public-private entity controlled by the State of Indiana, agreed to pay nearly \$8.3 million as a civil settlement relating to allegations of making false claims and false statements in connection with the E-Rate program. In addition to those allegations, the Department of Justice and the U.S. Attorney's Office for the Southern District of Indiana contended that Intelnet and the State of Indiana violated the E-Rate program's requirements by:
 - (i) charging inflated prices for services provided to Indiana schools and libraries.
 - (ii) falsifying invoices.
 - (iii) disregarding the requirement that schools and libraries make co-payments for the expenses charged to the E-rate program.
 - (iv) engaging in non-competitive bidding practices.
- In July 2006, Scott A. Federowicz pleaded guilty in the U.S. District Court in Hartford, Connecticut to two-counts of mail fraud in connection with a scheme to defraud the E-Rate program by obtaining funds for nonexistent/false business fronts and receiving a kickback from those funds. Federowicz was recruited by two Southwestern Bell Communications account managers to submit phony invoices for installing Internet access systems for the Hartford, New Haven, New London and Bridgeport school districts in Connecticut.
- In August 2006, a Federal grand jury in the United States District Court for the District of Maryland indicted Andre J. Hornsby on 16 counts that included wire fraud, mail fraud, witness and evidence tampering, and obstruction of justice for the purpose of defrauding the E-rate program in the Prince George's County Public Schools in Maryland by illegally circumventing numerous competitive procurement processes.

AUDIT AREAS

Conclusion

Our involvement in E-rate beneficiary audits and investigations has not lessened our concerns about fraud, waste, and abuse in Universal Service Fund programs. We remain committed to meeting our statutory responsibility to provide effective, independent oversight of all aspects of the Universal Service Fund program. We believe we are making significant progress toward achieving our goal of achieving an effective oversight program. As noted above, however, inadequate funding and personnel continue to impede our ability to provide effective, independent oversight of the E-rate program and the other programs that are financed through the Universal Service Fund.

Financial audits provide assurance as to whether an agency's financial statements fairly present the financial position of the FCC and its programs and the costs of its operations. In addition, the financial statement audit reports on the internal controls that support accurate financial reporting and compliance with applicable laws and regulations.

FINANCIAL AUDITS

In accordance with the Accountability of Tax Dollars Act of 2002, the FCC prepared consolidated financial statements for the 2006 fiscal year in accordance with Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. The Chief Financial Officers Act of 1990 (CFO Act), as amended, requires the FCC IG, or an independent external auditor selected by the Inspector General, to audit FCC financial statements in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. Under a contract supervised by the IG, Clifton Gunderson LLP (CG-LLP), an independent certified public accounting firm, is performing the audit of the FCC's FY 2006 consolidated financial statements in accordance with the aforesaid standards; OMB Bulletin No. 06-03, *Audit Requirements for Federal Financial Statement*, amended; and applicable sections of the U.S. Government Accountability Office (GAO)/President's Council on Integrity & Efficiency (PCIE) *Financial Audit Manual*.

AUDIT AREAS

This audit is currently in progress.

TELECOMMUNICATIONS RELAY SERVICE (TRS)

The TRS program became effective on July 26, 1993 as an interstate cost recovery plan to reimburse telecom-

munications common carriers for providing telephone voice relay translation services within the areas in which they offer voice services. Approximately \$470 million are contributed annually to a dozen providers by 2,800 common carriers which are paid by telephone customers through their monthly telephone bills. This program has not been subject to a comprehensive programmatic oversight audit by this office. In addition, the Commission has not been able to calculate the estimated percentage of erroneous payments for the TRS program.

The IG has initiated a series of audits that will provide the Commission and the IG with an independent and comprehensive examination and assessment of the FCC's TRS program administration and TRS provider compliance with 47 CFR §§ 64.601 - 64.605. During the current reporting period, we completed a risk assessment of the FCC's TRS oversight requirements, program management functions, and the operations of the TRS administrator. This project was completed April 26, 2006.



The next audit, currently underway, will amplify the initial effort by surveying the risk of improper reimbursements from the TRS Fund administered by NECA to providers and calculating the estimated percentage of erroneous payments. The objective of this audit is to determine the likelihood that reimbursements to providers were not based

on actual session minutes and/or allowable costs. We will review the internal controls of TRS providers and audit a sample of reimbursements. The results of this audit will constitute a survey that will help to determine the direction and depth of the compre-

AUDIT AREAS

hensive audit of records and assertions that will be needed to assess the representations made by NECA and the service providers.

The third audit will bookend the overall effort by conducting comprehensive audits. This will involve an audit of supporting documentation and other evidence at NECA and service providers to determine whether improper reimbursements were made as a result of incorrect session minutes and/or reimbursement rates. The service providers selected for audit received most of the reimbursements that were made during the last fiscal year. The results of this audit will determine the extent of improper payments and support the basis for any recovery of such payments.

We anticipate completing these audits by April, 2007.

The FCC has conducted auctions of licenses for electromagnetic spectrum since 1994. These auctions are open to any eligible company or individual that submits an application and required up-front payment, and is found to be a qualified bidder by the Commission. FCC auctions are conducted electronically and are accessible over the Internet. The Auctions and Spectrum Access Division within the FCC Wireless Telecommunications Bureau (WTB) leads the FCC auctions program. Extensive coordination with other divisions of the FCC is required. The OIG has audited several auctions functions over the years, but we have yet to focus a significant portion of our resources on auctions as a specific area of audit interest. In fiscal year 2007, we intend to audit additional auctions functions.

AUCTIONS

Our initial effort will involve a risk assessment of the auction program. The objectives of this assessment are to identify and catalog processes for: (i) administering the auction program; (ii) assessing associated vulnerabilities and risks; and (iii) determining whether the written policies, procedures and controls for mitigating risks are sufficient. The opinions obtained from this management risk evaluation will be used to determine whether additional audits targeted to specific risk areas within the Auctions

AUDIT AREAS

Program are necessary or desirable.

Forecasting and collecting auction fees is an essential aspect of the FCC's operations. In recent years, the Commission collected more than \$200,000,000 in auction fees each year. We will conduct an independent audit of the auction fee forecasting and collection processes, and determine whether the FCC's financial investment in the systems to automate this function have been sufficient to determine whether all applicable fees are being properly collected.

The Universal Licensing System (ULS) is a system used by the Wireless Telecommunications Bureau (WTB) to process hundreds of thousands of license applications annually. It has simplified the application and licensing processes and is intended to provide secure, world-wide access through the Internet. We will conduct an audit of the controls that are used to ensure that the Universal Licensing System's (ULS) intake, processing, storage, and reporting of data ensures that the information used by the FCC is accurate, complete and secure.

We have also selected the Purchase and Travelers Credit Card programs within the FCC auctions program for audit because of the potential for fraudulent, improper, and abusive use of the cards. The objectives of the audit are: (1) to determine whether the Purchase and Travelers Credit Card programs within the FCC auctions program are operated in accordance with prudent managerial principles; and (2) to assess the effectiveness of WTB's internal controls over the Purchase and Travelers Credit Card programs within the auctions program.

INFORMATION TECHNOLOGY AUDITS

Information Technology (IT) audits include audits of all aspects of the Commission's information systems. Beginning in 1994, the OIG conducted a variety of information system audits and special reviews including full scope audits of remote network access that also included

AUDIT AREAS

limited scope Internet penetration studies. In addition to the Uniform Licensing System audit discussed in the Auctions section of this report, we have several other audits in progress in the IT arena.

FY 2006 Federal Information Security Management Act (FISMA) Evaluation and Risk Assessment

The Federal Information Security Management Act (FISMA) requires that the IG perform an annual independent evaluation of the information security program of the FCC. The evaluation encompasses a complete review of the Commission's security program which includes security policies, security architecture, business continuity, security capital planning, critical infrastructure, and security program planning, management, and execution. This review is a risk assessment and is not a general controls review. The final product will be submitted to the Office of Management and Budget (OMB) for Fiscal Year 2006 and will be prepared in accordance with the reporting requirements mandated by FISMA.



In addition, we have modified our task order for the FY 2006 FISMA evaluation to include an independent assessment of FCC compliance with OMB Memorandum Number M-06-16, "Protection of Sensitive Agency Information," dated June 23, 2006. This independent assessment is being performed in accordance with the PCIE/ECIE Review Guide for Assessing Agency Efforts to Protect Sensitive Information.

Commission Registration System (CORES) Application Audit

The Commission Registration System (CORES) system was developed so that its users could more easily file applications, reports, and other documents with the FCC. CORES allows licensing and cable operation information to be more accessible to both FCC staff and to the public. The objective of this audit is to determine the extent and

AUDIT AREAS

effectiveness of security controls in the CORES application. We will evaluate the efficacy of security controls in CORES, including access controls, separation of duties, penetration testing, application audit trails, and application change controls.

PERFORMANCE AUDITS

Performance audits are systematic examinations that are conducted to assess the performance of a government program, activity or function so that corrective action can be taken, if appropriate. Performance audits

include audits of government contracts and grants with private sector organizations, as well as government and non-profit organizations that determine compliance with contractual terms, Federal Acquisition Regulations (FAR), and internal contractual administration.

In addition to the oversight of the Telecommunications Relay Service (TRS), Information Technology audits and the auctions audits that will be conducted under performance audit standards, the following audits are in progress or have been completed.

Audit of Regulatory Fee Collections

Collection of fees is an essential financial function. Because of the criticality of the fee collection process, and the significant financial investment that has to been made in the systems to automate this function, the IG determined that audit work is warranted. This audit will examine the regulatory fee collection process to ascertain whether the Commission can be reasonably confident that all applicable regulatory fees are being collected. The OIG will review both manual and automated controls over the regulatory fee collection process. We will also review a statistical sample of regulated entities to determine if the Commission has been collecting all fees due. Audit planning has been initiated for this activity.

AUDIT AREAS

Incurring Cost Contract Audits

The primary objective of an incurred cost audit is to examine a contractor's cost representations and express an opinion as to whether those representations are reasonable, and whether cost representations were properly incurred under the contract and not prohibited by the contract, statute or regulation, or by decision of, or agreement with, the contracting officer. Incurred cost audits are performed at the request of the Commission's Contracts and Purchasing Center.

On August 10, 2006 we issued a report that was initially prepared by the Defense Contract Audit Agency (DCAA), that described DCAA's review of the final indirect cost proposal submitted by NeuStar, Inc. to establish indirect costs rates for FY 2004 incurred costs claimed under FCC contract number CON01000016. These rates apply primarily to flexibly-priced contracts. DCAA's audit disclosed no improper findings. As a consequence, and upon further review, we concluded that NeuStar's indirect rates for January 1, 2004 through December 31, 2004 could properly be used for contract and/or task order closeouts.

In addition, DCAA is currently under contract and auditing the Titan Corporation's FY 2004 incurred costs for FCC's contracts CON0100008 and CON01000009.



INVESTIGATIONS

SUMMARY OF INVESTIGATIONS

Investigations pursued by this office are frequently initiated as a result of allegations received through the OIG hotline, or from FCC managers and employees who contact the OIG directly. Allegations can be, and frequently are, made anonymously. Investigations may also be predicated upon audit or inspection findings of fraud, waste, abuse, corruption, or mismanagement by FCC employees, contractors, and/or subcontractors or through referrals from other governmental agencies.

Recently, this office has been working on an upsurge of cyber crime investigations. The OIG works directly with Federal criminal authorities, supporting either their investigations, or having these agencies support this office with resources unavailable within the FCC. Upon receiving an allegation of an administrative, civil, or criminal violation, the OIG usually conducts a preliminary inquiry to determine if an investigation is warranted. Investigations may involve possible violations of Federal regulations regarding employee responsibilities and conduct, Federal criminal law, and other regulations and statutes pertaining to the activities of the Commission. Investigative findings may lead to criminal or civil prosecution, or administrative action, or all of the foregoing.

The OIG also receives complaints from the general public, both private citizens and commercial enterprises, about the manner in which the FCC executes its programs and conducts its oversight responsibilities. All complaints are examined to determine whether there is any basis for OIG audit or investigative action. If nothing is alleged that is within the jurisdiction of the IG, the complaint is usually referred to the appropriate FCC bureau or office for response directly to the complainant. The OIG continues to serve as a facilitator with respect to responses to complaints that are outside the jurisdiction of this office. Finally, matters may be referred to this office for investigative action from other governmental entities, such as the Government Accountability Office, the Office of Special Counsel, or various congressional offices.

INVESTIGATIONS

Forty-eight (48) cases were pending from the prior period. Thirty-five (35) of those cases involve the Commission's Universal Service Fund (USF) program and

have been referred to the Federal Bureau

of investigation (FBI) and/or the Department of Justice. An additional eleven (11) non-USF and four (4) USF related complaints were received during the current reporting period. Over the last six months, five (5) cases, two (2) USF and three (3) non-USF related, have been closed. A total of fifty-eight (58) cases are still pending, of which thirty-seven (37) relate to the USF program. The OIG continues to monitor, coordinate and/or support activities regarding those thirty-seven (37) investigations. The investigations pertaining to the pending twenty-one (21) non-USF cases are ongoing.

ACTIVITY DURING THIS PERIOD

STATISTICS

Cases pending as of March 31, 2006	48
New cases	15
Cases closed	5
Cases pending as of September 30, 2006	58

- Pursuant to the direction of Chairman Kevin Martin and requests from Senators Barbara Boxer, Byron Dorgan, and Ron Wyden, and Members of Congress, the IG initiated an inquiry into allegations of inappropriate conduct by individuals at the FCC, past and present, concerning the possible destruction and/or suppression of draft studies or reports regarding localism and media ownership. Localism addresses, generally, the issue of whether locally-owned television or radio stations produce more local news. Media ownership addresses, generally, multiple media ownership concen-

SIGNIFICANT

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tration in market-defined outlets. The aforementioned Senators further requested a comprehensive investigation regarding past and present practices within the FCC to suppress any materials contrary to any individual's desired expression. This investigation is ongoing.



- During this period, the OIG initiated an inquiry into the alleged theft and destruction of FCC data. The data were not confidential, but did contain personal identifying information in the form of e-mail addresses. This office was able to recover all of the data, and there is no indication at this time that the data were released to, or otherwise valuable to, the public. The OIG is currently working with Federal law enforcement agencies to determine what Federal laws have been violated, if any.
- During this period, the Assistant Inspector General for Investigations initiated an inquiry into allegations from a foreign government regarding possible cyber attacks upon an election website initiated from within the FCC. The alleged cyber attack was during the run-up to local elections. Working with the Federal Bureau of Investigation, this office was able to conclude that the attacks were not initiated from within the FCC, and that aspect of the investigation was officially closed.
- During this period, the Assistant Inspector General for Investigations assisted the Federal Trade Commission in getting a temporary restraining order issued to halt the unfair business practices of an online check processing firm. The online firm allowed checks to be created and sent to any bank account without verifying that the customer had the authority to write checks drawn on that account. The FCC, and several other Federal agencies, had to fend off multiple attempts to procure Federal monies via this online activity. The OIG is monitoring this case.
- During this period, the Assistant Inspector General for Investigations initiated an

INVESTIGATIONS

inquiry into allegations of improper use of a Federal government workstation by a FCC employee by downloading, saving, and viewing pornographic material. During the course of the investigation, the individual under investigation left the FCC. The matter was thereafter officially closed.

- During this period, the Assistant Inspector General for Investigations initiated an inquiry into allegations of cyber attacks upon FCC personnel from outside the Commission. One such attack involved the distribution of private, non-public information of an FCC employee. This office is currently working with the Department of Homeland Security and various State agencies to resolve this investigation, which is ongoing.
- During this period, the Assistant Inspector General for Investigations initiated an inquiry into a harassment allegation from within the FCC. This investigation is ongoing.
- In the previous reporting period, the IG described an inquiry into allegations of procurement fraud involving an FCC employee. This inquiry resulted in a criminal fraud referral to the Federal Bureau of Investigation, but we have not received any further updates. We will continue to monitor this referral until the statute of limitations expires.
- In the prior reporting period, the IG described an inquiry into allegations of improper conduct by a Commission employee with respect to the possession of private information concerning a group of Commission employees. That inquiry has yielded no further information. This investigation will be kept open until we finish working with Federal law enforcement agencies in this matter.

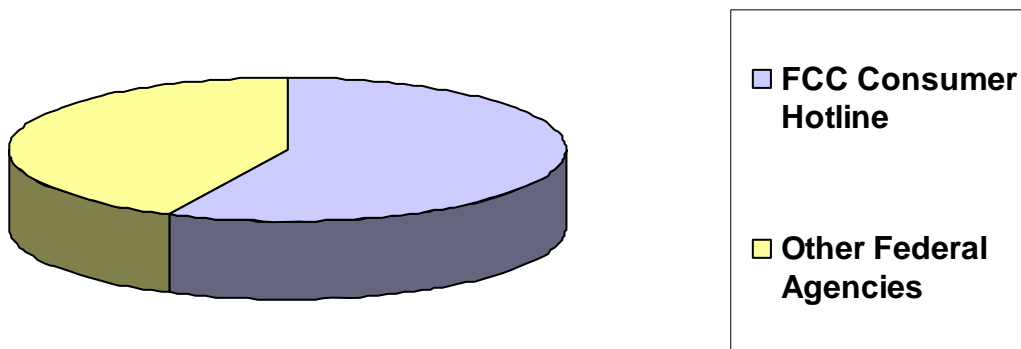
In addition to the foregoing, the OIG continues to coordinate and provide assistance to Federal civil and law enforcement entities with respect to investigations pertaining to infractions within the Universal Service Fund program of the Commission.

INVESTIGATIONS

OIG HOTLINE

During this reporting period, the OIG Hotline technician received numerous calls to the published hotline numbers of (202) 418-0473 and 1-888-863-2244 (toll free). The OIG Hotline continues to be a vehicle by which Commission employees and parties external to the FCC can contact the OIG to speak with a trained Hotline technician. Callers who have general questions or concerns not specifically related to the missions or functions of the OIG office are referred to the FCC Consumer Center at 1-888-225-5322. In addition, the OIG also refers calls that do not fall within its jurisdiction to other entities, such as other FCC offices, Federal agencies and local or state governments. Examples of calls referred to the Consumer Center or other FCC offices include complaints pertaining to customers' phone service and local cable providers, long-distance carrier slamming, interference, or similar matters within the program responsibility of other FCC bureaus and offices. During this reporting period, we received 130 Hotline calls. The majority of these calls were forwarded to the FCC Consumer Center (74 calls) and the balance of calls were referred to other Federal agencies, primarily the Federal Trade Commission (51 calls).

Hotline Calls Record
April 1, 2006 - September 30, 2006



INVESTIGATIONS

Report Fraud, Waste or Abuse to:

Office of the Inspector General
Federal Communications Commission

CALL

Hotline: (202) 418-0473

or

(888) 863-2244

www.fcc.gov/oig



You are always welcome to write or visit.

Federal Communications Commission

Portals II Building

REPORTING REQUIREMENTS



Reporting Requirements of the Inspector General Act

REPORTING REQUIREMENTS

The following summarizes the Office of Inspector General response to the 12 specific reporting requirements set forth in Section 5(a) of the Inspector General Act of 1978, as amended.

1. A description of significant problems, abuses, and deficiencies relating to the administration of programs and operations of such establishment disclosed by such activities during the reporting period.

Please refer to the Section of this report entitled "Universal Service Fund" on pages 8 through 18.

2. A description of the recommendations for corrective action made by the Office during the reporting period with respect to significant problems, abuses, or deficiencies identified pursuant to paragraph (1).

Please refer to the Section of this report entitled "Universal Service Fund" on pages 8 through 18.

3. An identification of each significant recommendation described in previous semiannual reports on which corrective action has not yet been completed.

No significant recommendations remain outstanding.

4. A summary of matters referred to authorities, and the prosecutions and convictions which have resulted.

Please refer to the Section of this report entitled "Universal Service Fund" on pages 8 through 18.

One non-USF case has been referred to the Department of Justice during this reporting period.

5. A summary of each report made to the head of the establishment under section (6)

REPORTING REQUIREMENTS

(b) (2) during the reporting period.

No report was made to the Chairman of the FCC under section (6) (b) (2) during this reporting period.

6. A listing, subdivided according to subject matter, of each audit report issued by the office during the reporting period, and for each audit report, where applicable, the total dollar value of questioned costs (including a separate category for the dollar value of unsupported costs) and the dollar value of recommendations that funds be put to better use.

Each audit report issued during the reporting period is listed according to subject matter and described in the "Audit Areas" section of this report.

7. A summary of each particularly significant report.

Each significant audit and investigative report issued during the reporting period is summarized within the body of this report.

8. Statistical tables showing the total number of audit reports with questioned costs and the total dollar value of questioned costs.

The required statistical table can be found at Table I to this report.

9. Statistical tables showing the total number of audit reports with recommendations that funds be put to better use and the total dollar value of such recommendations.

The required statistical table can be found at Table II to this report.

10. A summary of each audit report issued before the commencement of the reporting period for which no management decision has been made by the end of the reporting

REPORTING REQUIREMENTS

period (including the date and title of each such report), an explanation of the reasons why such a management decision has not been made, and a statement concerning the desired timetable for achieving a management decision on each such report.

No audit reports fall within this category.

11. A description and explanation of the reasons for any significant revised management decision made during the reporting period.

No management decisions fall within this category.

12. Information concerning any significant management decision with which the Inspector General is in disagreement.

No management decisions fall within this category.

13. Information described under section 05(b) of the Federal Financial Management Improvement Act of 1996.

No reports with this information have been issued during this reporting period.



REPORTING REQUIREMENTS

Table I: OIG Reports With Questioned Costs

Inspector General Reports With Questioned Costs	Number of Reports	Questioned Costs	Unsupported Costs
A. For which no management decision has been made by the commencement of the reporting period.	—	—	—
B. Which were issued during the reporting period.	36	\$11,502,220	—
C. For which a management decision was made during the reporting period.	36	\$11,502,220	—
(i) Dollar value of disallowed costs	—	—	—
(ii) Dollar value of costs not disallowed	—	—	—
D. For which no management decision has been made by the end of the reporting period.	—	—	—
Reports for which no management decision was made within six months of issuance.	—	—	—

REPORTING REQUIREMENTS

Table II: OIG Reports With Recommendations That Funds Be Put To Better Use

Inspector General Reports With Recommendations That Funds Be Put To Better Use	Number of Reports	Dollar Value
A. For which no management decision has been made by the commencement of the reporting period.	—	—
B. Which were issued during the reporting period.	—	—
C. For which a management decision was made during the reporting period.	—	—
(i) Dollar value of disallowed costs	—	—
(ii) Dollar value of costs not disallowed	—	—
D. For which no management decision has been made by the end of the reporting period.	—	—
Reports for which no management decision was made within six months of issuance.	—	—



Back Row: Vanessa Lamb, Roy Connor, David Hunt, Harold Shrewsberry, Thomas Cline, Kim Bumstead, Kevin Beynum, Keith Bernard, William Hill, Jon Stover Front Row: William Garay, Whitney Brooks, Makysa Moton, Kent Nilsson, Carrie-Lee Early, Carla Conover, Sharon Spencer, Beth Engelmann, Randal Skalski

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